

REC'D TN
REGULATORY AUTH.
BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE 58

IN RE:

OFFICE OF THE
EXECUTIVE SECRETARY

UNITED CITIES GAS PETITION
FOR APPROVAL OF NEW
OR REVISED FRANCHISE
AGREEMENTS WITH KINGSPORT,
BRISTOL, MORRISTOWN AND
MAURY COUNTY

No. 00-00562

MEMORANDUM IN SUPPORT OF
THE CITY OF MORRISTOWN'S
MOTION TO INTERVENE

Comes the City of Morristown, Tennessee, a municipal corporation, by and through counsel, and files with it Motion to Intervene this Memorandum of Law.

I. Background. In 1999, the City of Morristown (hereinafter the "City") entered into negotiations with United Cities Gas Company ("United Cities Gas") with respect to franchise rights within the City of Morristown. On March 10, 2000, the City's ordinance number 3022 (the "Franchise Agreement"), granting a fifteen (15) year franchise to United Cities Gas, was finalized. Prior to the issuance of this franchise, in December, 1979, the City had granted to United Cities Gas a twenty (20) year franchise to operate exclusively within the City of Morristown. As the expiration of the franchise drew near in December 1999, the City explored its options and considered other avenues to provide gas services within its boundaries. The City had received several complaints regarding the current service provided by United Cities Gas and was

seeking alternate potential avenues to correct the existing perceived deficiencies. As a result of intense negotiation, a new franchise was ultimately granted to United Cities, which included new provisions such as the maintenance of an office within the City and certain default and cure provisions. The Franchise Agreement also contained a provision for a five percent (5%) gross receipts franchise fee to be paid to the City.

II. Validity of the Franchise Agreement. Pursuant to Tenn.CodeAnn. §6-2-201, the City of Morristown has the express power to grant to any association or corporation a franchise for public utilities and public services to be furnished to the municipality. Such power embraces the power to grant exclusive franchises. *Id.* It has been stated that "this power, by clear implication, includes the power to levy a franchise fee." Tenn.Op.Atty.Gen.No. 98-233. Further, the Tennessee Supreme Court has stated that, acting in its proprietary capacity, "a municipality may exact a charge for the use of its rights-of-way, but in its governmental capacity, it may only act through an exercise of its police power to regulate specific activity or to defray the cost of providing services or benefit to the party paying the fee." *City of Tullahoma v. Bedford County*, 938 S.W.2d 408 (Tenn. 1997). Moreover, it has been held that a municipality operates its utilities in a proprietary or individual capacity and not in its legislative or governmental capacity. *Batson v. Pleasant View Utility District*, 592 S.W.2d 578 (Tenn.Ct.App. 1979). Thus, the rules that control a private individual or corporate business generally apply to a municipality operating a utility in a proprietary or individual capacity. *Id.*

III. Execution of the Franchise Agreement and the imposition of the fee provided therein is a valid, proprietary function exercised by the City of Morristown and not a governmental function.

A municipal corporation possesses two kinds of power, one governmental or public and the other private. *State v. Knoxville*, 115 Tenn. 175, 90 S.W. 289 (1905). A city exercises its legislative or governmental powers when it does something with respect to the public duty generally and it exercises its private or proprietary powers when it does something affecting the corporate body alone and not the public generally. *Gillespie v. Rhea County*, 191 Tenn. 487, 235 S.W.2d 4 (1950).

In *Lewis v. Nashville Gas and Heating Company*, 40 S.W.2d 409 (Tenn. 1931), the Tennessee Supreme Court was faced with the question of whether payments provided in a gas franchise agreement whereby the gas company agreed to pay to the City five percent of its gross receipts from the sale of gas were imposed by the City in the exercise of its governmental power, either to tax or regulate. The Court held that an annual charge on gross receipts imposed by the city in exchange for the use of its streets was not one imposed in the exercise of either the governmental power to tax or the police power to regulate. Discussing the nature of the charge, the Court stated that the city was authorized by statute to prescribe the terms and conditions upon which the gas company might enter and establish its business. Further, the Court stated that the contract was entered into:

"through negotiations with the gas company, and the obligation, voluntarily assumed by it, was not the result of the exercise of a governmental power, but of contract which both parties could make (*City of Lancaster v. Briggs*, 118

Mo. App. 570, 96 S. W. 314), and the annual payments prescribed by section 14 of the ordinance were compensation to be paid the city for the exercise of the franchise, conditionally granted by the state, subject to assent of the city as proprietor of its streets. Among others, this proposition is well supported by the following authorities: Hanford Gas Co. v. City, 163 Cal. 108, 124 P. 727; Byrne v. Chicago Gen. Ry. Co., 169 Ill. 75, 48 N. E. 703; Alleghany City v. Railway, 159 Pa. 411, 28 A. 202; City of Mitchell v. Dakota Telephone Co., 25 S. D. 409, 127 N. W. 582; Jamestown v. Home Telephone Co., 125 App. Div. 1, 109 N. Y. S. 297; Portsmouth v. Virginia Railway, 141 Va. 54, 126 S. E. 362, 39 A. L. R. 1510. See, also, 19 R. C. L. p. 1153, 427, where it is said: "One of the conditions which a municipal corporation can lawfully attach to the grant of a franchise is the payment of money; and the payment need not be such as is imposed upon all others similarly situated, as in the case of a tax, or the equivalent of the cost of inspection and replacement, as in the case of a license fee imposed under the police power, but may be a definite sum arbitrarily selected, and if the company does not wish to pay it need not accept the franchise."

Lewis at 412-413.

Further, in discussing the issue of whether the City was involved in the exercise of police powers and/or taxing powers, the Court stated that "Since the payments prescribed by ... the ordinance result from the contract voluntarily engaged in and which both parties could make, the question as to an exercise of governmental power by the city is not involved." *Id* at 413. See Also *Nashville Gas and Heating Co. v. City of Nashville*, 152 S.W.2d 229 (Tenn. 1941). Thus, where a franchise fee is the result of negotiations between the City and an individual entity, the City is acting in its proprietary capacity.

In *City of Chattanooga v. BellSouth Telecommunications, Inc., et al.*, 2000 WL 122199 (Tenn.Ct.App. Jan.26, 2000) , relied upon by the Consumer Advocate, the Court was faced with a similar issue to that considered in *Lewis v. Nashville Gas and Heating Company*. That is, the issue before the Court was whether a franchise fee imposed by the City of Chattanooga violated state law as either an impermissible tax or as an ultra vires act of police power by the City. *Id.* at 1. The *Bellsouth* Court determined that, under the facts of the case, Chattanooga was not acting in its proprietary capacity. Instead, it was acting in its governmental capacity because it was attempting, through ordinance, to revoke or impair rights previously given to third parties by a prior enactment. *Id.* at 1. The Court stated that "the City may not modify the franchise by imposing a fee under the City's proprietary functions." *Id.* at 2.

Specifically, in 1996 the City of Chattanooga enacted an ordinance amending its existing ordinance relative to telecommunication services within the city, which attempted to require any party wishing to provide telecommunication services within the City to obtain a franchise from the City and to pay a fee in the amount of 5% of its gross revenue. Further, any such franchisee was required to furnish to the City, for its exclusive use, an underground duct, pole space, four fiber optic fibers, and engineering assistance for initial hookup by the City.

Prior to passage of the amendment, the City had granted franchises to two of the defendant companies and/or their predecessors. Accordingly, the amendment was classified by the Court as an attempt to modify the preexisting franchises. Thus, such an attempt by the City was

not a permissible "proprietary function" or a valid method of imposing a new fee upon existing and future telecommunication suppliers. Because of this, the city must have necessarily been acting in its governmental capacity, attempting to do what it could not do as a matter of law in its proprietary capacity. In order to be valid as an exercise of its governmental functions or its police power, the charge imposed by the amendment must have been one that bore a reasonable relation to the objective to be accomplished.

As such, the *BellSouth* case does not overrule the case law in Tennessee which allows a city, in its proprietary function, to charge a franchise fee of the type at issue before this Agency. Quite to the contrary, the *BellSouth* case cites and confirms the Tennessee common law allowing such franchise fees. However, based upon the facts in *BellSouth*, the City of Chattanooga was not attempting to exercise proprietary powers in the negotiation of a franchise agreement with an individual provider. Instead, Chattanooga attempted to unilaterally modify existing contracts and to regulate future activity within the City via ordinance. Thus, the facts of the *BellSouth* case are entirely distinguishable, in that Chattanooga, as a matter of law, was not acting, and could not so act, in its proprietary capacity. In other words, the language in *BellSouth*, without expressly saying so, impliedly states that Chattanooga was attempting, through the use of governmental powers, to do what it could not permissibly do using its proprietary powers which are constrained by the law of contracts and other common and statutory law in Tennessee. Accordingly, the holding in *BellSouth* simply does not

apply where a City is entering into a new franchise agreement and not attempting to change or modify an existing franchise by and through an exercise of police power.

On the other hand, where a City, such as Morristown in this case, has imposed such a fee as a result of intense negotiation for the issuance of an exclusive franchise right to provide gas service within its boundaries and for the use of its rights-of-way, the franchise fee is valid as a proper exercise of the municipality's proprietary functions.

IV. Conclusion.

Based upon the foregoing, the City of Morristown seeks permission to intervene in the above-styled action, so that it may adequately represent its interest in the Franchise Agreement at issue. It is the City of Morristown's position that said Franchise Agreement was executed by it and United Cities Gas Company as a result of an arms length transaction which falls well within the City's powers in its proprietary capacity. As such, the parties thereto as governed by the rules that control private individuals and businesses generally and are fairly bound by the negotiated terms of the Agreement.

Respectfully submitted this ____ day of November, 2001.

CITY OF MORRISTOWN

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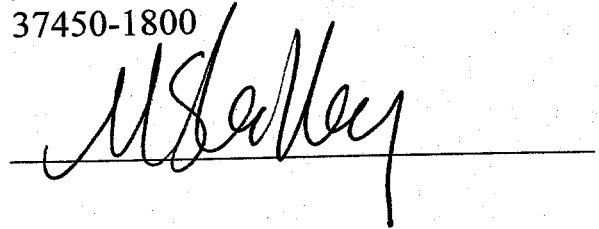
CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been mailed, postage prepaid, to the following parties of interest this 27th day of November, 2001:

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A handwritten signature in black ink, appearing to read "M. S. Kelley", is written over a horizontal line.